

# PERAC AUDIT REPORT



Salem



Contributory Retirement System

JAN. 1, 2010 - DEC. 31, 2012





# TABLE OF CONTENTS

Letter from the Executive Director .....	I
Explanation of Findings and Recommendations.....	2
Statement of Ledger Assets and Liabilities.....	6
Statement of Changes in Fund Balances .....	7
Statement of Receipts.....	8
Statement of Disbursements.....	9
Investment Income .....	10
Schedule of Allocation of Investments Owned.....	11
Supplementary Investment Regulations .....	12
Notes to Financial Statements:	
Note 1 - Summary of Plan Provisions .....	13
Note 2 - Significant Accounting Policies .....	20
Note 3 - Supplementary Membership Regulations.....	22
Note 4 - Administration of the System .....	24
Note 5 - Actuarial Valuation and Assumptions.....	25
Note 6 - Membership Exhibit.....	26
Note 7 – Premises Owned and Occupied .....	27



# PERAC

COMMONWEALTH OF MASSACHUSETTS | PUBLIC EMPLOYEE RETIREMENT ADMINISTRATION COMMISSION

JOSEPH E. CONNARTON, *Executive Director*

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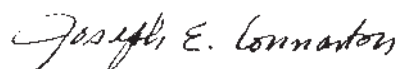
July 15, 2014

The Public Employee Retirement Administration Commission has completed an examination of the Salem Retirement System pursuant to G.L. c. 32, § 21. The examination covered the period from January 1, 2010 to December 31, 2012. This audit was conducted in accordance with the accounting and management standards established by the Public Employee Retirement Administration Commission in regulation 840 CMR 25.00. Additionally, all supplementary regulations approved by PERAC and on file at PERAC are listed in this report.

In our opinion, the financial records are being maintained and the management functions are being performed in conformity with the standards established by the Public Employee Retirement Administration Commission with the exception of those noted in the findings presented in this report.

In closing, I acknowledge the work of examiner James Tivnan who conducted this examination, and express appreciation to the Board of Retirement and staff for their courtesy and cooperation.

Sincerely,



Joseph E. Connarton  
Executive Director





# EXPLANATION OF FINDINGS AND RECOMMENDATIONS

## **I. Regular Compensation Defined**

The auditor sampled payrolls from all five employer units to determine that member's rate, base deductions, and 2% additional deductions were accurate. We reviewed a list of pay types or codes that indicated whether they were used in the determination of base regular compensation used for retirement contributions. We observed a number of Pay Codes reported by the City of Salem as qualifying for retirement purposes included some descriptions that referenced "OT", "Incentive", "Detail", "Extra", "Clothing" and "Uniform". We requested clarification of the description and use of these codes.

**Recommendation:** The system should insist that all employer units advise the Salem Retirement Board of all new payroll codes initiated by the unit payroll officers. The Retirement Board must be the ultimate authority to determine compensation that qualifies for retirement contributions subject to and within the guidelines prescribed in 840 CMR 15.03. A complete payroll register should be periodically obtained from each of the employer units to monitor and confirm compliance. This function will provide an additional layer of internal financial control to confirm that contributions are accurate and benefits are earned within the established rules.

### **Board Response:**

The Salem Retirement Board recognizes the importance of ensuring that retirement deductions are assessed only on compensation which meets the definition of regular compensation, pursuant to 840 CMR 15.03, as well as the most up to date PERAC auditing standards. The Salem Retirement System has met with officials from the City of Salem as part of an ongoing conversation aimed at keeping the City of Salem informed of the definition of regular compensation. City officials have confirmed that there has been little to no exposure to these payroll codes, many of which are obsolete, and that they will be deleted going forward. Similar conversations will be scheduled between the Salem Retirement Board and our other member units. The Salem Retirement Board appreciates the recommendation made by the PERAC examiner and will continue to provide training on the definition of regular compensation to all five of the member units that fall under the jurisdiction of the Salem Retirement Board.

## **2. Additional 2% Contributions Deducted From Payroll**

The PERAC auditor sampled payrolls from all five employer units. Issues with the calculation of the additional 2% contribution for compensation in excess of \$30,000 applied on an annualized basis were observed. It is common for some employees of the North Shore Regional Vocational High School as well as the City of Salem school department to change their contract terms upon resumption of the new school year in September. We identified five members affected whose new contract terms resulted in compensation at a level requiring additional 2% contributions. None of these members had the requisite deductions initiated prior to identification by the auditor.

**Recommendation:** PERAC Memo #43/1999 provides the definitive guidance on withholding for the additional 2% contribution for compensation in excess of \$30,000 applied on an annualized basis. The Retirement Board must be notified of substantive changes to the terms and conditions of employment involving its members. A copy of the contract terms specific to paraprofessional employees as well as all collectively bargained agreements must be provided regularly to the Retirement Board.

## EXPLANATION OF FINDINGS AND RECOMMENDATIONS (Continued)

### **Board Response:**

The Salem Retirement Board recognizes the importance of ensuring that the requisite additional 2% contribution on compensation in excess of \$30,000 is assessed properly and consistently. The Salem Retirement System has met with the Business Manager from the City of Salem school department and has participated in ongoing conversations with the North Shore Regional Vocational High School Business Manager in an effort to address this finding. The Salem Retirement Board appreciates the recommendation made by the PERAC examiner and will be furnished with copies of contract terms going forward. The Salem Retirement System plans to routinely compare deduction reports with payroll records, as well as contracts/collective bargaining agreements, for all five of the member units that fall under the jurisdiction of the Salem Retirement Board.

### **3. Confirming the Accurate Determination of Benefits**

The PERAC auditor reviewed the calculation of retirement benefits for a reasonable sample of recent retirees. Notably absent from the file contents were any source reference confirming the payroll records used to determine the key element of the formula used in the determination of these benefits. The cumulative effect that the prior findings (#1 and #2) advance serves to undermine the reliability of the definition of regular compensation used by the system. Contributions received by the system should not be the primary criteria used as a basis for calculating benefits for retirees of the system.

**Recommendation:** Actual payroll records should be obtained, referenced and maintained in the retiree files to more formally document the essential components used in the determination of retiree benefits.

### **Board Response:**

Since 2013, the Salem Retirement System has routinely requested complete payroll records for prospective retirees as part of the benefit calculation process. The Salem Retirement System has recently been granted “read-only” access to the City of Salem’s Munis payroll database, which will allow the Salem Retirement System to view payroll records while consuming fewer resources. A request for similar access will be made to the Salem Retirement Board’s four other member units. This information will be added to all retiree files.

### **4. Expenses**

During a review of the expenses of the system, it was observed that:

- The system paid a vendor twice from a duplicate invoice
- The system paid an annual service contract twice within the same annual period
- Payments to the same vendor for essentially the same service were applied to different general ledger accounts
- The descriptive detail provided by the general ledger was generally insufficient to identify the vendor, service or product obtained without reference to the actual source documentation



## EXPLANATION OF FINDINGS AND RECOMMENDATIONS (Continued)

- Reimbursement requests for travel, lodging, parking, tolls and associated costs are not reported on a standard form that describes the purpose and justification for the reimbursement

**Recommendation:** The Executive Director should more formally document the expense procedures of the retirement system. They should be specific for any agreement handling the billing requirements for a particular vendor. Standards for adequate documentation prior to payment should be defined. All vendors must conform to the statutory requirement that requires a majority of Board members to approve payment of all invoices. Payment should be authorized exclusively from original invoices. Vendor specific activity should initiate general ledger transactions. A more complete reconciliation protocol should be initiated to limit payments for duplicate services.

**Board Response:**

The Salem Retirement Board agrees with the PERAC examiner's finding. The Salem Retirement System has recouped the duplicate payment made on an annual service contract from 2012 and was able to determine that the vendor invoice that had appeared to have been paid twice had simply been incorrectly attached to two separate payments. The vendor was able to produce the second invoice, which reconciled to the amount paid. The Executive Director has instituted the use of "sub-accounts" in an effort to better distinguish various disbursements, as well as receipts, and has expanded on account descriptions. The Executive Director has also implemented a new process for reimbursement requests.

### **5. System Administration**

At the Board meeting held on November 28, 2012 the Executive Director presented a sick time and vacation time unused buyback calculation that was approved by the Board. Given the specific personal interest and advantage that two staff members had in such a calculation, the Board would have been better served to delegate this calculation to an independent third party from another retirement Board or alternative resource. The PERAC Auditor observed the distribution of these funds was made without using the Board payroll application. No withholding for applicable Federal or State income taxes was observed.

**Recommendation:** The distribution of funds to individuals within the jurisdiction of the Salem Retirement Board must only be made under the specific regulatory criteria established by the Board, the U. S. Treasury regulations and similar payroll guidance. Distributions classified as payroll that are not included in the payroll application and reported to the proper authority are not valid distributions and cannot be supported as a qualified use of retirement system funds. It is incumbent on the system to conform to the existing rules for all payroll distributions, tax withholding, filing and reporting regulations.

**Board Response:**

The Salem Retirement Board recognizes the importance of performing its due diligence with regard to distributions to its staff members, and while the Salem Retirement Board did provide oversight for the sick and vacation leave buyout presented by the former Executive Director, the Board

## EXPLANATION OF FINDINGS AND RECOMMENDATIONS (Continued)

appreciates the recommendation made by the PERAC examiner. The Salem Retirement System currently has one remaining employee who is eligible to receive a sick and vacation leave buyout and, at the time of her retirement, this calculation will be delegated to an independent third party from another retirement board so as to avoid any potential conflict of interest. The retirement benefit calculation for the Executive Director of the Salem Retirement System, as well as any calculation regarding payment to be made in consideration of remaining unused vacation time, shall also be delegated to an independent third party from another retirement board so as to avoid any potential conflict of interest.

### **6. Board Member Attendance**

A review of meeting attendance by Board members revealed a member missed four monthly meetings in each of the years during the current audit period. The result is an attendance rate for a Board member that was below the seventy-five percent minimum considered reasonable.

**Recommendation:** Attendance at Board meetings is an obligation that must be fulfilled by all Board members. Board members are obligated by their fiduciary duty to the retirement system to attend meetings regularly. The Board should consider adjusting the schedule of Board meetings in order to better accommodate its members.

### **Board Response:**

The Salem Retirement Board members recognize their obligation to attend regular meetings and they take their fiduciary duty seriously. The Board has taken measures to improve their overall attendance rate, such as voting to allow remote participation when warranted and to adjust the monthly meeting schedule to a time and date that is more accommodating to each Board member's schedule.

### **FINAL DETERMINATION:**

***PERAC Audit staff will follow up in six (6) months to ensure appropriate actions have been taken regarding all findings.***

## STATEMENT OF LEDGER ASSETS AND LIABILITIES

	AS OF DECEMBER 31,		
	2012	2011	2010
<b>Net Assets Available For Benefits:</b>			
Cash	\$8,236,949	\$7,009,017	\$6,318,743
Short Term Investments	1,478,300	1,326,533	1,240,460
Pooled Alternative Investment Funds	141,242	191,598	243,826
Pooled Real Estate Funds	462,902	564,672	571,850
PRIT Core Fund	96,438,473	85,018,605	85,296,150
Accounts Receivable	294,530	425,604	301,733
Premises and Equipment, Net	100,781	103,906	107,031
Accounts Payable	(5,250)	(5,533)	(7,620)
<b>Total</b>	<u>\$107,147,927</u>	<u>\$94,634,402</u>	<u>\$94,072,292</u>
<b>Fund Balances:</b>			
Annuity Savings Fund	\$38,417,169	\$36,546,297	\$35,125,673
Annuity Reserve Fund	8,677,627	8,888,413	8,758,966
Pension Fund	199,953	68,447	161,090
Military Service Fund	756	755	754
Expense Fund	0	0	0
Pension Reserve Fund	<u>59,852,421</u>	<u>49,130,490</u>	<u>50,025,809</u>
<b>Total</b>	<u>\$107,147,927</u>	<u>\$94,634,402</u>	<u>\$94,072,292</u>

## STATEMENT OF CHANGES IN FUND BALANCES

	Annuity Savings Fund	Annuity Reserve Fund	Pension Fund	Military Service Fund	Expense Fund	Pension Reserve Fund	Total All Funds
Beginning Balance (2010)	\$33,318,732	\$9,064,848	\$328,219	\$751	\$0	\$40,659,725	\$83,372,276
Receipts	3,446,984	260,542	10,461,740	2	736,324	9,359,807	24,265,399
Interfund Transfers	(1,081,675)	1,075,398	0	0	0	6,277	0
Disbursements	(558,368)	(1,641,822)	(10,628,868)	0	(736,324)	0	(13,565,383)
Ending Balance (2010)	35,125,673	8,758,966	161,090	754	0	50,025,809	94,072,292
Receipts	3,763,855	267,520	10,932,841	2	782,900	(890,749)	14,856,368
Interfund Transfers	(1,687,882)	1,692,453	0	0	0	(4,570)	(0)
Disbursements	(655,348)	(1,830,525)	(11,025,484)	0	(782,900)	0	(14,294,257)
Ending Balance (2011)	36,546,297	8,888,413	68,447	755	0	49,130,490	94,634,402
Receipts	3,796,140	259,110	11,350,058	1	924,718	10,721,931	27,051,957
Interfund Transfers	(1,337,441)	1,337,441	0	0	0	0	0
Disbursements	(587,827)	(1,807,336)	(11,218,551)	0	(924,718)	0	(14,538,432)
Ending Balance (2012)	<u>\$38,417,169</u>	<u>\$8,677,627</u>	<u>\$199,953</u>	<u>\$756</u>	<u>\$0</u>	<u>\$59,852,421</u>	<u>\$107,147,927</u>

# STATEMENT OF RECEIPTS

FOR THE PERIOD ENDING DECEMBER 31,			
	2012	2011	2010
<b>Annuity Savings Fund:</b>			
Members Deductions	\$3,331,519	\$3,282,127	\$3,131,624
Transfers from Other Systems	273,800	331,698	124,824
Member Make Up Payments and Re-deposits	146,119	71,265	77,876
Investment Income Credited to Member Accounts	<u>44,702</u>	<u>78,765</u>	<u>112,660</u>
Sub Total	<u>3,796,140</u>	<u>3,763,855</u>	<u>3,446,984</u>
<b>Annuity Reserve Fund:</b>			
Investment Income Credited to the Annuity Reserve Fund	<u>259,110</u>	<u>267,520</u>	<u>260,542</u>
Sub Total	<u>259,110</u>	<u>267,520</u>	<u>260,542</u>
<b>Pension Fund:</b>			
3 (8) (c) Reimbursements from Other Systems Received from Commonwealth for COLA and Survivor Benefits	153,139	154,480	155,646
Pension Fund Appropriation	255,540	273,881	314,507
Settlement of Workers' Compensation Claims	10,941,379	10,497,479	9,991,587
	<u>0</u>	<u>7,000</u>	<u>0</u>
Sub Total	<u>11,350,058</u>	<u>10,932,841</u>	<u>10,461,740</u>
<b>Military Service Fund:</b>			
Investment Income Credited to the Military Service Fund	<u>1</u>	<u>2</u>	<u>2</u>
Sub Total	<u>1</u>	<u>2</u>	<u>2</u>
<b>Expense Fund:</b>			
Investment Income Credited to the Expense Fund	<u>924,718</u>	<u>782,900</u>	<u>736,324</u>
Sub Total	<u>924,718</u>	<u>782,900</u>	<u>736,324</u>
<b>Pension Reserve Fund:</b>			
Interest Not Refunded	2,338	2,362	5,441
Miscellaneous Income	0	0	361
Excess Investment Income (Loss)	<u>10,719,592</u>	<u>(893,111)</u>	<u>9,354,005</u>
Sub Total	<u>10,721,931</u>	<u>(890,749)</u>	<u>9,359,807</u>
<b>Total Receipts, Net</b>	<u>\$27,051,957</u>	<u>\$14,856,368</u>	<u>\$24,265,399</u>

# STATEMENT OF DISBURSEMENTS

FOR THE PERIOD ENDING DECEMBER 31,			
	2012	2011	2010
<b>Annuity Savings Fund:</b>			
Refunds to Members	\$303,475	\$350,864	\$357,871
Transfers to Other Systems	<u>284,352</u>	<u>304,484</u>	<u>200,497</u>
Sub Total	<u>587,827</u>	<u>655,348</u>	<u>558,368</u>
<b>Annuity Reserve Fund:</b>			
Annuities Paid	1,807,336	1,753,644	1,641,822
Option B Refunds	<u>0</u>	<u>76,882</u>	<u>0</u>
Sub Total	<u>1,807,336</u>	<u>1,830,525</u>	<u>1,641,822</u>
<b>Pension Fund:</b>			
Pensions Paid:			
Regular Pension Payments	7,518,162	7,531,977	7,241,393
Survivorship Payments	623,406	487,879	469,611
Ordinary Disability Payments	59,174	59,108	75,316
Accidental Disability Payments	2,057,865	1,970,652	1,893,133
Accidental Death Payments	555,657	565,715	539,305
Section 101 Benefits	41,092	45,318	53,968
3 (8) (c) Reimbursements to Other Systems	<u>363,196</u>	<u>364,834</u>	<u>356,142</u>
Sub Total	<u>11,218,551</u>	<u>11,025,484</u>	<u>10,628,868</u>
<b>Expense Fund:</b>			
Board Member Stipend	15,000	15,000	15,000
Salaries and Benefits	293,207	219,137	215,570
Legal Expenses	12,803	225	825
Travel Expenses	11,562	4,839	2,862
Administrative Expenses	27,272	22,286	27,478
Actuarial Services	19,500	0	17,000
Education and Training	2,810	1,080	1,620
Furniture and Equipment	2,174	5,515	12,330
Management Fees	490,808	452,300	385,819
Custodial Fees	12,750	21,000	15,750
Service Contracts	22,945	27,937	28,843
Fiduciary and Other Insurance	10,762	10,455	10,103
Depreciation	<u>3,125</u>	<u>3,125</u>	<u>3,125</u>
Sub Total	<u>924,718</u>	<u>782,900</u>	<u>736,324</u>
<b>Total Disbursements</b>	<u>\$14,538,432</u>	<u>\$14,294,257</u>	<u>\$13,565,383</u>

# INVESTMENT INCOME

	FOR THE PERIOD ENDING DECEMBER 31,		
	2012	2011	2010
<b>Investment Income Received From:</b>			
Cash	\$21,951	\$35,172	\$39,462
Short Term Investments	4,286	0	0
Equities	9,423	741	9,248
Pooled or Mutual Funds	<u>2,940,517</u>	<u>2,648,793</u>	<u>2,273,278</u>
<b>Total Investment Income</b>	<u>2,976,176</u>	<u>2,684,706</u>	<u>2,321,988</u>
<b>Plus:</b>			
Realized Gains	2,345,760	2,696,288	2,407,611
Unrealized Gains	12,341,754	8,735,614	15,758,305
Interest Due and Accrued - Current Year	<u>0</u>	<u>0</u>	<u>119</u>
Sub Total	<u>14,687,514</u>	<u>11,431,903</u>	<u>18,166,035</u>
<b>Less:</b>			
Realized Loss	(110,865)	(269,218)	(1,782,084)
Unrealized Loss	(5,604,703)	(13,611,196)	(8,242,400)
Interest Due and Accrued - Prior Year	<u>0</u>	<u>(119)</u>	<u>(6)</u>
Sub Total	<u>(5,715,567)</u>	<u>(13,880,533)</u>	<u>(10,024,490)</u>
<b>Net Investment Income</b>	<u>11,948,123</u>	<u>236,075</u>	<u>10,463,533</u>
<b>Income Required:</b>			
Annuity Savings Fund	44,702	78,765	112,660
Annuity Reserve Fund	259,110	267,520	260,542
Military Service Fund	1	2	2
Expense Fund	<u>924,718</u>	<u>782,900</u>	<u>736,324</u>
<b>Total Income Required</b>	<u>1,228,531</u>	<u>1,129,186</u>	<u>1,109,528</u>
Net Investment Income	<u>11,948,123</u>	<u>236,075</u>	<u>10,463,533</u>
Less: Total Income Required	<u>1,228,531</u>	<u>1,129,186</u>	<u>1,109,528</u>
<b>Excess Income (Loss) To The Pension Reserve Fund</b>	<u>\$10,719,592</u>	<u>(\$893,111)</u>	<u>\$9,354,005</u>

## SCHEDULE OF ALLOCATION OF INVESTMENTS OWNED

(percentages by category)

AS OF DECEMBER 31, 2012		
	MARKET VALUE	PERCENTAGE OF TOTAL ASSETS
Cash	\$8,236,949	7.7%
Short Term Investments	1,478,300	1.4%
Pooled Alternative Investment Funds	141,242	0.1%
Pooled Real Estate Funds	462,902	0.4%
PRIT Core Fund	<u>96,438,473</u>	<u>90.3%</u>
<b>Grand Total</b>	<b><u>\$106,757,866</u></b>	<b><u>100.0%</u></b>

For the year ending December 31, 2012, the rate of return for the investments of the Salem Retirement System was 12.73%. For the five-year period ending December 31, 2012, the rate of return for the investments of the Salem Retirement System averaged 0.90%. For the 28-year period ending December 31, 2012, since PERAC began evaluating the returns of the retirement systems, the rate of return on the investments of the Salem Retirement System was 8.06%.

The composite rate of return for all retirement systems for the year ending December 31, 2012 was 13.84%. For the five-year period ending December 31, 2012, the composite rate of return for the investments of all retirement systems averaged 1.83%. For the 28-year period ending December 31, 2012, since PERAC began evaluating the returns of the retirement systems, the composite rate of return on the investments of all retirement systems averaged 9.27%.



## SUPPLEMENTARY INVESTMENT REGULATIONS

The Salem Retirement System has more than ninety per-cent of their funds invested in the PRIT fund managed by the PRIM Board. Certain residual investment agreements related to holdings of Pooled Alternative Investments and Pooled Real Estate Funds could not be abrogated and remain under the care and custody of the Salem Retirement System. Such residual investments generally consist of limited partnership subscriptions for a specific term. These terms are fixed for a period usually not to exceed ten years. As a result, the supplemental investment regulations that were previously approved by the Public Employee Retirement Administration Commission and remain on file at PERAC have been effectively rescinded, except as they pertain to the residual holdings referenced above. A complete list of these regulations is available upon written request and can be accessed via the internet at the following address:

<http://www.mass.gov/perac/investsup/salemintsup.html>

# NOTES TO FINANCIAL STATEMENTS

## NOTE I – SUMMARY OF PLAN PROVISIONS

The plan is a contributory defined benefit plan covering all Salem Retirement System member unit employees deemed eligible by the retirement board, including the City of Salem, the Salem and Beverly Water Supply Board, the South Essex Sewerage District, the Salem Housing Authority, the North Shore Regional Vocational High School as well as the Salem Contributory Retirement System with the exception of school department employees who serve in a teaching capacity. The Teachers' Retirement Board administers the pensions of such school employees.

### ADMINISTRATION

There are 105 contributory retirement systems for public employees in Massachusetts. Each system is governed by a retirement board and all boards, although operating independently, are governed by Chapter 32 of the Massachusetts General Laws. This law in general provides uniform benefits, uniform contribution requirements and a uniform accounting and funds structure for all systems.

### PARTICIPATION

Participation is mandatory for all full-time employees. Eligibility with respect to part-time, provisional, temporary, seasonal or intermittent employment is governed by regulations promulgated by the retirement board, and approved by PERAC. Membership is optional for certain elected officials.

There are 4 classes of membership in the retirement system, but one of these classes, Group 3, is made up exclusively of the State Police. The other 3 classes are as follows:

#### **Group 1:**

General employees, including clerical, administrative, technical and all other employees not otherwise classified.

#### **Group 2:**

Certain specified hazardous duty positions.

#### **Group 4:**

Police officers, firefighters, and other specified hazardous positions.

## NOTES TO FINANCIAL STATEMENTS (Continued)

### MEMBER CONTRIBUTIONS

Member contributions vary depending on the most recent date of membership:

Prior to 1975:	5% of regular compensation
1975 - 1983:	7% of regular compensation
1984 to 6/30/96:	8% of regular compensation
7/1/96 to present:	9% of regular compensation
1979 to present:	an additional 2% of regular compensation in excess of \$30,000.

In addition, members of Group 1 who join the system on or after April 2, 2012 will have their withholding rate reduced to 6 % after achieving 30 years of creditable service.

### RATE OF INTEREST

Interest on regular deductions made after January 1, 1984 is a rate established by PERAC in consultation with the Commissioner of Banks. The rate is obtained from the average rates paid on individual savings accounts by a representative sample of at least 10 financial institutions.

### RETIREMENT AGE

The mandatory retirement age for some Group 2 and Group 4 employees is age 65. Most Group 2 and Group 4 members may remain in service after reaching age 65. Group 4 members who are employed in certain public safety positions are required to retire at age 65. There is no mandatory retirement age for employees in Group 1.

### SUPERANNUATION RETIREMENT

A person who became a member before April 2, 2012 is eligible for a superannuation retirement allowance (service retirement) upon meeting the following conditions:

- completion of 20 years of service, or
- attainment of age 55 if hired prior to 1978, or if classified in Group 4, or
- attainment of age 55 with 10 years of service, if hired after 1978, and if classified in Group 1 or 2

A person who became a member on or after April 2, 2012 is eligible for a superannuation retirement allowance (service retirement) upon meeting the following conditions:

- attainment of age 60 with 10 years of service if classified in Group 1, or
- attainment of age 55 with 10 years of service if classified in Group 2, or
- attainment of age 55 if classified in Group 4.

## NOTES TO FINANCIAL STATEMENTS (Continued)

### AMOUNT OF BENEFIT

A member's annual allowance is determined by multiplying average salary by a benefit rate related to the member's age and job classification at retirement, and the resulting product by his creditable service. The amount determined by the benefit formula cannot exceed 80% of the member's highest three year (or five year as discussed below) average salary. For veterans as defined in G.L. c. 32, s. 1, there is an additional benefit of \$15 per year for each year of creditable service, up to a maximum of \$300.

For employees who become members after January 1, 2011, regular compensation is limited to 64% of the federal limit found in 26 U.S.C. 401(a)(17). In addition, regular compensation will be limited to prohibit "spiking" of a member's salary to increase the retirement benefit.

- For persons who became members prior to April 2, 2012, Average Salary is the average annual rate of regular compensation received during the 3 consecutive years that produce the highest average, or, if greater, during the last 3 years (whether or not consecutive) preceding retirement.
- For persons who became members on or after April 2, 2012, Average Salary is the average annual rate of regular compensation received during the 5 consecutive years that produce the highest average, or, if greater, during the last 5 years (whether or not consecutive) preceding retirement.
- The Benefit Rate varies with the member's retirement age. For persons who became members prior to April 2, 2012 the highest rate of 2.5% applies to Group 1 employees who retire at or after age 65, Group 2 employees who retire at or after age 60, and to Group 4 employees who retire at or after age 55. A .1% reduction is applied for each year of age under the maximum age for the member's group. For Group 2 employees who terminate from service under age 55, the benefit rate for a Group 1 employee shall be used.
- For persons who became members on or after April 2, 2012 and retire with less than 30 years of creditable service, the highest rate of 2.5% applies to Group 1 employees who retire at or after age 67, Group 2 employees who retire at or after age 62, and to Group 4 employees who retire at or after age 57. A .15% reduction is applied for each year of age under the maximum age for the member's group.
- For persons who became members on or after April 2, 2012 and retire with more than 30 years of creditable service, the highest rate of 2.5% applies to Group 1 employees who retire at or after age 67, Group 2 employees who retire at or after age 62, and to Group 4 employees who retire at or after age 55. A .125% reduction is applied for each year of age under the maximum age for the member's group.

### DEFERRED VESTED BENEFIT

A participant who has attained the requisite years of creditable service can elect to defer his or her retirement until a later date. Certain public safety employees cannot defer beyond age 65. All participants must begin to receive a retirement allowance or withdraw their accumulated deductions no later than April 15 of the calendar year following the year they reach age 70½.

## NOTES TO FINANCIAL STATEMENTS (Continued)

### WITHDRAWAL OF CONTRIBUTIONS

Member contributions may be withdrawn upon termination of employment. The interest rate for employees who first become members on or after January 1, 1984 who voluntarily withdraw their contributions with less than 10 years of service will be 3%. Interest payable on all other withdrawals will be set at regular interest.

### DISABILITY RETIREMENT

The Massachusetts Retirement Plan provides 2 types of disability retirement benefits:

#### ORDINARY DISABILITY

**Eligibility:** Non-veterans who become totally and permanently disabled by reason of a non-job related condition with at least 10 years of creditable service (or 15 years creditable service in systems in which the local option contained in G.L. c. 32, s.6(1) has not been adopted).

Veterans with ten years of creditable service who become totally and permanently disabled by reason of a non-job related condition prior to reaching “maximum age”. “Maximum age” applies only to those employees classified in Group 4 who are subject to mandatory retirement.

**Retirement Allowance:** For persons who became members prior to April 2, 2012, the benefit is equal to the accrued superannuation retirement benefit as if the member was age 55. If the member is a veteran, the benefit is 50% of the member’s final rate of salary during the preceding 12 months, plus an annuity based upon accumulated member contributions plus credited interest. If the member is over age 55, he or she will receive not less than the superannuation allowance to which he or she is entitled.

For persons in Group 1 who became members on or after April 2, 2012, the benefit is equal to the accrued superannuation retirement benefit as if the member was age 60. If the member is a veteran, the benefit is 50% of the member’s final rate of salary during the preceding 12 months, plus an annuity based upon accumulated member contributions plus credited interest. If the member is over age 60, he or she will receive not less than the superannuation allowance to which he or she would have been entitled had they retired for superannuation.

For persons in Group 2 and Group 4 who became members on or after April 2, 2012, the benefit is equal to the accrued superannuation retirement benefit as if the member was age 55. If the member is a veteran, the benefit is 50% of the member’s final rate of salary during the preceding 12 months, plus an annuity based upon accumulated member contributions plus credited interest. If the member is over age 55, he or she will receive not less than the superannuation allowance to which he or she would have been entitled had they retired for superannuation.

## NOTES TO FINANCIAL STATEMENTS (Continued)

### ACCIDENTAL DISABILITY

**Eligibility:** Applies to members who become permanently and totally unable to perform the essential duties of the position as a result of a personal injury sustained or hazard undergone while in the performance of duties. There are no minimum age or service requirements.

**Retirement Allowance:** 72% of salary plus an annuity based on accumulated member contributions, with interest. This amount is not to exceed 100% of pay. For those who became members in service after January 1, 1988 or who have not been members in service continually since that date, the amount is limited to 75% of pay. There is an additional pension of \$774.36 per year (or \$312.00 per year in systems in which the local option contained in G.L. c. 32, s. 7(2)(a)(iii) has not been adopted), per child who is under 18 at the time of the member's retirement, with no age limitation if the child is mentally or physically incapacitated from earning. The additional pension may continue up to age 22 for any child who is a full time student at an accredited educational institution. For systems that have adopted Chapter 157 of the Acts of 2005, veterans as defined in G.L. c. 32, s. 1 receive an additional benefit of \$15 per year for each year of creditable service, up to a maximum of \$300.

### ACCIDENTAL DEATH

**Eligibility:** Applies to members who die as a result of a work-related injury or if the member was retired for accidental disability and the death was the natural and proximate result of the injury or hazard undergone on account of which such member was retired.

**Allowance:** An immediate payment to a named beneficiary equal to the accumulated deductions at the time of death, plus a pension equal to 72% of current salary and payable to the surviving spouse, dependent children or the dependent parent, plus a supplement of \$774.36 per year, per child (or \$312.00 per year in systems in which the local option contained in G.L. c. 32, s. 9(2)(d)(ii) has not been adopted), payable to the spouse or legal guardian until all dependent children reach age 18 or 22 if a full time student, unless mentally or physically incapacitated.

The surviving spouse of a member of a police or fire department or any corrections officer who, under specific and limited circumstances detailed in the statute, suffers an accident and is killed or sustains injuries while in the performance of his duties that results in his death, may receive a pension equal to the maximum salary for the position held by the member upon his death. In addition, an eligible family member may receive a one time payment of \$100,000.00 from the State Retirement Board. This lump sum payment is also available to the family of a public prosecutor in certain, limited circumstances.

## NOTES TO FINANCIAL STATEMENTS (Continued)

### DEATH AFTER ACCIDENTAL DISABILITY RETIREMENT

Effective November 7, 1996, Accidental Disability retirees were allowed to select Option C at retirement and provide a benefit for an eligible survivor. For Accidental Disability retirees prior to November 7, 1996, who could not select Option C, if the member's death is from a cause unrelated to the condition for which the member received accidental disability benefits, a surviving spouse will receive an annual allowance of \$6,000. For Systems that accept the provisions of Section 28 of Chapter 131 of the Acts of 2010, the amount of this benefit is \$9,000. For Systems that accept the provisions of Section 63 of Chapter 139 of the Acts of 2012, the amount of this benefit is \$12,000.

### DEATH IN ACTIVE SERVICE

**Allowance:** An immediate allowance equal to that which would have been payable had the member retired and selected Option C on the day before his or her death. For a member who became a member prior to April 2, 2012 whose death occurred prior to the member's superannuation retirement age, the age 55 benefit rate is used. For a member classified in Group 1 who became a member on or after April 2, 2012 whose death occurred prior to the member's superannuation retirement age, the age 60 benefit rate is used. If the member died after age 60, the actual age is used. For a member classified in Group 2 or Group 4, whose death occurred prior to the member's minimum superannuation retirement age, the benefit shall be calculated using an age 55 age factor. The minimum annual allowance payable to the surviving spouse of a member in service who dies with at least two years of creditable service is \$3,000 unless the retirement system has accepted the local option increasing this minimum annual allowance to \$6,000, provided that the member and the spouse were married for at least one year and living together on the member's date of death.

The surviving spouse of such a member in service receives an additional allowance equal to the sum of \$1,440 per year for the first child and \$1,080 per year for each additional child until all dependent children reach age 18 or 22 if a full time student, unless mentally or physically incapacitated.

### COST OF LIVING

If a system has accepted Chapter 17 of the Acts of 1997, and the Retirement Board votes to pay a cost of living increase (COLA) for that year, the percentage is determined based on the increase in the Consumer Price Index used for indexing Social Security benefits, but cannot exceed 3.0%. Section 51 of Chapter 127 of the Acts of 1999, if accepted, allows boards to grant COLA increases greater than that determined by CPI but not to exceed 3.0%. Only a certain portion of a retiree's total allowance is subject to a COLA. The total COLA for periods from 1981 through 1996 is paid for by the Commonwealth of Massachusetts.

Under the provisions of Chapter 32, Section 103(j) inserted by Section 19 of Chapter 188 of the Acts of 2010, systems may increase the maximum base on which the COLA is calculated in multiples of \$1,000. For many years the COLA base was calculated based upon the first \$12,000 of a retiree's allowance. Now the maximum base upon which the COLA is calculated varies from system to system. . Each increase in the base must be accepted by a majority vote of the Retirement Board and approved by the legislative body.

## NOTES TO FINANCIAL STATEMENTS (Continued)

### METHODS OF PAYMENT

A member may elect to receive his or her retirement allowance in one of 3 forms of payment.

**Option A:** Total annual allowance, payable in monthly installments, commencing at retirement and terminating at the member's death.

**Option B:** A reduced annual allowance, payable in monthly installments, commencing at retirement and terminating at the death of the member, provided, however, that if the total amount of the annuity portion received by the member is less than the amount of his or her accumulated deductions, including interest, the difference or balance of his accumulated deductions will be paid in a lump sum to the retiree's beneficiary or beneficiaries of choice.

**Option C:** A reduced annual allowance, payable in monthly installments, commencing at retirement. At the death of the retired employee, 2/3 of the allowance is payable to the member's designated beneficiary (who may be the spouse, or former spouse who is has not remarried, child, parent, sister, or brother of the employee) for the life of the beneficiary. For members who retired on or after January 12, 1988, if the beneficiary pre-deceases the retiree, the benefit payable increases (or "pops up" to Option A) based on the factor used to determine the Option C benefit at retirement. For members who retired prior to January 12, 1988, if the System has accepted Section 288 of Chapter 194 of the Acts of 1998 and the beneficiary pre-deceases the retiree, the benefit payable "pops up" to Option A in the same fashion. The Option C became available to accidental disability retirees on November 7, 1996.

### ALLOCATION OF PENSION COSTS

If a member's total creditable service was partly earned by employment in more than one retirement system, the cost of the "pension portion" is allocated between the different systems pro rata based on the member's service within each retirement system. If a member received regular compensation concurrently from two or more systems on or after January 1, 2010, and was not vested in both systems as of January 1, 2010, such a pro-ration will not be undertaken. This is because such a person will receive a separate retirement allowance from each system.



## NOTES TO FINANCIAL STATEMENTS (Continued)

### NOTE 2 - SIGNIFICANT ACCOUNTING POLICIES

The accounting records of the System are maintained on a calendar year basis in accordance with the standards and procedures established by the Public Employee Retirement Administration Commission.

Cash accounts are considered to be funds on deposit with banks and are available upon demand.

Short Term Investments are highly liquid investments that will mature within twelve months from the date of acquisition.

Investments are reported at their fair value. Securities traded on recognized exchanges are valued at the most recent sales price at year end. If no sale was reported, the mean of the bid and asked price is used when available, or the most recent bid price. Mutual, commingled and pooled funds are valued based on the net asset or unit value at year end. Real estate and alternative investments are valued based on estimates provided by the managers of those respective investments. Purchases and sales of securities are reflected on the date the trade is initiated. Realized gain or loss is largely based on the difference between the cost or the value at the prior year end and the funds realized upon liquidation. Dividend income is generally recorded when received. Interest income is recorded as earned on an accrual basis. Income from alternative investments is recorded as reported by the managing partner. Appreciation or depreciation in the value of investments consists of the unrealized gains and losses reported as the difference between the previous period and the current value.

The system makes estimates and assumptions that affect the reported values of assets and liabilities and the reported amounts added and deducted during the reporting periods. The fair value of real estate and alternative investment holdings are generally estimated in the absence of reliable exchange values. The actual funds realized upon liquidation may differ from these estimates.

The provisions of Massachusetts General Laws Chapter 32, § 23 (2) generally govern the investment practices of the system. The Board primarily relies upon the investment strategy of the PRIM Board to maintain their progress toward full funding of the system. That strategy seeks to balance the exposure to common deposit and investment risks related to custody, credit concentrations, interest rate and foreign currency fluctuations.

Operating expenses include the ordinary and necessary cost of investment and professional services and the other miscellaneous administrative expenses of the system.

## NOTES TO FINANCIAL STATEMENTS (Continued)

The Annuity Savings Fund is the fund in which members' contributions are deposited. Voluntary contributions, re-deposits, and transfers to and from other systems, are also accounted for in this fund. Members' contributions to the fund earn interest at a rate determined by PERAC. Interest for some members who withdraw with less than ten years of service is transferred to the Pension Reserve Fund. Upon retirement, members' contributions and interest are transferred to the Annuity Reserve Fund. Dormant account balances must be transferred to the Pension Reserve Fund after a period of ten years of inactivity.

The Annuity Reserve Fund is the fund to which a member's account is transferred upon retirement from the Annuity Savings Fund and Special Military Service Credit Fund. The annuity portion of the retirement allowance is paid from this fund. Interest is credited monthly to this fund at the rate of 3% annually on the previous month's balance.

The Special Military Service Credit Fund contains contributions and interest for members while on a military leave for service in the Armed Forces who will receive creditable service for the period of that leave.

The Expense Fund contains amounts transferred from investment income for the purposes of administering the retirement system.

The Pension Fund contains the amounts appropriated by the governmental units as established by PERAC to pay the pension portion of each retirement allowance.

The Pension Reserve Fund contains amounts appropriated by the governmental units for the purposes of funding future retirement benefits. Any profit or loss realized on the sale or maturity of any investment or on the unrealized gain of a market valued investment as of the valuation date is credited to the Pension Reserve Fund. Additionally, any investment income in excess of the amount required to credit interest to the Annuity Savings Fund, Annuity Reserve Fund, and Special Military Service Credit Fund is credited to this Reserve account.

The Investment Income Account is credited with all income derived from interest and dividends of invested funds. At year-end the interest credited to the Annuity Savings Fund, Annuity Reserve Fund, Expense Fund, and Special Military Service Credit Fund is distributed from this account and the remaining balance is transferred to the Pension Reserve Fund.

## NOTES TO FINANCIAL STATEMENTS (Continued)

### NOTE 3 - SUPPLEMENTARY MEMBERSHIP REGULATIONS

The Salem Retirement System submitted the following supplementary membership regulations, which were approved by the Public Employee Retirement Administration Commission on:

December 8, 2011

#### Membership

- A. Employees of all member units of the Salem Retirement System who are regularly employed in a permanent position for a minimum of 20 hours per week and who earn a minimum of \$5,000 per year must become members of the System.
- B. Employees of all units of the Salem Retirement System who are provisional, seasonal, or temporary, and who are regularly employed in a position for a minimum of 20 hours per week for a period of six consecutive months, and who earn a minimum of \$5,000 per year, must become members of the system at the conclusion of the six-month period. Such member shall be allowed to purchase prior non-membership service.
- C. Employees of all member units of the Salem Retirement System who are employed less than 20 hours per week, are ineligible for membership.
- D. Employees and appointed officials of all member units of the Salem Retirement System who earn less than \$5,000 per year are ineligible for membership.
- E. Employees who do not qualify for membership in the Salem Retirement system and later become members in another Chapter 32 retirement system and then seek to "buyback" their prior part-time service, Salem Retirement will not accept liability for this service.

December 8, 2011

#### Creditable Service

- A. Members of the Salem Retirement System who earn less than \$5,000 per year and who established membership prior to July 1, 2009 shall continue to be members of the system. The regular compensation of such member shall be subject to retirement withholdings, but such member shall not accrue creditable service after July 1, 2009, except that such member who on said date was serving in an elected or appointed term of office or employment shall continue to be credited with service until the expiration of his term of office or employment, or until July 1, 2012, whichever first occurs.
- B. Members of the Salem Retirement System shall be credited with one year of service for each year of employment of not less than 20 hours per week, or yearly proportion thereof. If the members' hours of employment fall below 20 hours per week, the member shall be credited with one-half year of creditable service, or yearly proportion thereof.
- C. It is up to the applicant to provide all essential information to the Retirement Board for all creditable service.

## NOTES TO FINANCIAL STATEMENTS (Continued)

### NOTE 3 - SUPPLEMENTARY MEMBERSHIP REGULATIONS (Continued)

January 19, 2011

#### Buyback Policy

The policy of the Salem Contributory Retirement Board in regards to buybacks, makeup and veteran's credit is as follows:

**FOR MILITARY CREDIT:** This payment is made, when necessary, as a lump sum payment before retirement by either a cash payment or from a deferred comp plan.

**BUYBACK OF PREVIOUS REFUNDS:** Lump sum payment at any time with interest.

**MAKEUP FOR PREVIOUS SERVICE FOR WHICH NO DEDUCTIONS WERE EVER TAKEN:** Lump sum payment at any time with interest.

All members are encouraged to make deductions to a deferred compensation plan so that their payments will be pretax.

The Retirement Board does not accept payment plans.

#### Travel Regulations:

The Salem Retirement System has adopted Travel Supplemental Regulations under the provisions of G.L. c. 7, § 50 and G.L. c. 32, § 21(4). Regulations available upon written request, and are also available on the PERAC website <http://www.mass.gov/perac/Salem>).

## NOTES TO FINANCIAL STATEMENTS (Continued)

### NOTE 4 - ADMINISTRATION OF THE SYSTEM

The System is administered by a five-person Board of Retirement consisting of the Finance Director/Auditor who shall be a member ex-officio, a second member appointed by the governing authority, a third and fourth member who shall be elected by the members in or retired from the service of such system, and a fifth member appointed by the other four board members.

Ex-officio Member: Sarah Stanton

Appointed Member: Kimberley Driscoll                      Until a successor is appointed

Elected Member: Sally Hayes, Chairperson              Term Expires: 6/3/2016

Elected Member: John Burke, Jr.                      Term Expires: 12/3/2014

Appointed Member: Robert Lutts                      Term Expires: 1/2/2016

The Board members are required to meet at least once a month. The Board must keep a record of all of its proceedings. The Board must annually submit to the appropriate authority an estimate of the expenses of administration and cost of operation of the system. The board must annually file a financial statement of condition for the system with the Executive Director of PERAC.

The investment of the system's funds is the responsibility of the Board. All retirement allowances must be approved by the Retirement Board. The PERAC Actuary performs verification prior to payment, unless the system has obtained a waiver for superannuation calculations allowing them to bypass this requirement. All expenses incurred by the System must be approved by a majority vote of the Board. Payments shall be made only upon vouchers signed by two persons designated by the Board.

The following retirement board members and employees are bonded by an authorized agent representing a company licensed to do business in Massachusetts as follows:

Treasurer - Custodian:	)	Coverage provided to a limit of \$10,000,000 under a
Ex-officio Member:	)	master MACRS sponsored policy issued through
Elected Members:	)	Travelers Casualty & Surety Co. of America
Appointed Members:	)	Deductible \$50,000. Separate fidelity coverage
		pertaining to ERISA/Crime to a limit of
Staff Employees:	)	\$1,000,000 issued through Travelers Casualty and
		Surety Company, deductible \$10,000.

## NOTES TO FINANCIAL STATEMENTS (Continued)

### NOTE 5 - ACTUARIAL VALUATION AND ASSUMPTIONS

The most recent actuarial valuation of the System was prepared by The Segal Company as of January 1, 2012.

The actuarial liability for active members was	\$104,380,391
The actuarial liability for inactive participants	2,515,234
The actuarial liability for retired members and beneficiaries was	<u>107,450,738</u>
The total actuarial liability was	\$214,346,363
System assets as of that date were	<u>106,806,161</u>
The unfunded actuarial liability was	<u>\$107,540,202</u>
 The ratio of system's assets to total actuarial liability was	 49.8%
As of that date the total covered employee payroll was	\$37,076,549

The normal cost for employees on that date was 9.3% of payroll

The normal cost for the employer was (including administrative expenses) 6.5% of payroll

The principal actuarial assumptions used in the valuation are as follows:

Investment Return:	8.0% per annum
Rate of Salary Increase:	5.00% per annum

### GASB STATEMENT NO. 25, DISCLOSURE INFORMATION AS OF JANUARY 1, 2012

Actuarial Valuation Date	Actuarial Value of Assets ( a )	Actuarial Accrued Liability ( b )	Unfunded AAL (UAAL) ( b-a )	Funded Ratio ( a/b )	Covered Payroll ( c )	UAAL as a % of Cov. Payroll ( ( b-a)/c )
1/1/2012	\$106,806,161	\$214,346,363	\$107,540,202	49.8%	\$37,076,549	290.0%
1/1/2010	\$100,046,731	\$193,470,036	\$93,423,305	51.7%	\$34,583,002	270.1%
1/1/2008	\$99,998,471	\$179,382,299	\$79,383,828	55.7%	\$34,410,002	230.7%

## NOTES TO FINANCIAL STATEMENTS (Continued)

### NOTE 6 - MEMBERSHIP EXHIBIT

	2003	2004	2005	2006	2007	2008	2009	2010	2011	2012
<b>Retirement in Past Years</b>										
Superannuation	54	21	5	14	15	21	23	13	23	19
Ordinary Disability	0	2	0	0	0	1	3	0	0	0
Accidental Disability	3	3	1	1	3	2	2	2	0	2
<b>Total Retirements</b>	57	26	6	15	18	24	28	15	23	21
 Total Retirees, Beneficiaries and Survivors	646	640	619	633	625	618	588	578	579	563
 Total Active Members	839	883	840	834	867	882	845	878	870	868
<b>Pension Payments</b>										
Superannuation	\$5,532,260	\$6,272,261	\$6,369,684	\$6,509,618	\$6,736,404	\$6,649,104	\$7,075,214	\$7,241,393	\$7,531,977	\$7,518,162
Survivor/Beneficiary	467,567	464,813	480,580	443,552	443,037	450,578	446,266	469,611	487,879	623,406
Ordinary Disability	125,572	129,197	123,133	128,096	101,586	82,859	91,766	75,316	59,108	59,174
Accidental Disability	1,438,846	1,488,077	1,537,994	1,565,494	1,757,609	1,790,298	1,859,607	1,893,133	1,970,652	2,057,865
Other	<u>741,454</u>	<u>818,390</u>	<u>926,104</u>	<u>916,111</u>	<u>892,554</u>	<u>1,009,837</u>	<u>1,127,952</u>	<u>949,416</u>	<u>975,868</u>	<u>959,945</u>
<b>Total Payments for Year</b>	<u>\$8,305,699</u>	<u>\$9,172,738</u>	<u>\$9,437,495</u>	<u>\$9,562,871</u>	<u>\$9,931,190</u>	<u>\$9,982,676</u>	<u>\$10,600,805</u>	<u>\$10,628,868</u>	<u>\$11,025,484</u>	<u>\$11,218,551</u>

## NOTES TO FINANCIAL STATEMENTS (Continued)

### NOTE 7 - PREMISES OWNED AND OCCUPIED

The Salem Retirement Board is located in a commercial condominium unit situated in downtown Salem. The unit was acquired by purchase in April, 2005. The unit was acquired after leasing the same unit for the period from 1999 to March, 2005. The original cost was \$125,000. The original purchase was charged directly to the expense fund in calendar year 2005. In 2009, the purchase was capitalized to comply with the provisions of GASB #34. The useful life of this asset is estimated to be forty years. The unit is being depreciated using the straight line method over this period. The annual depreciation associated with this office condominium is \$3,125. The costs of normal maintenance and repairs that do not add to the value or materially extend its useful life are not capitalized. There is no mortgage or other short term or long term debt associated with this acquisition. The retirement board conducts the normal course of its administrative activities, counsels' members and retirees, maintains the records and holds the required regular public Board meetings from this location.









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# PERAC

COMMONWEALTH OF MASSACHUSETTS | PUBLIC EMPLOYEE RETIREMENT ADMINISTRATION COMMISSION

PHILIP Y. BROWN, ESQ., *Chairman*

JOSEPH E. CONNARTON, *Executive Director*

Auditor SUZANNE M. BUMP | KATHLEEN M. FALLON | KATE FITZPATRICK | JAMES M. MACHADO | ROBERT B. MCCARTHY | JENNIFER F. SULLIVAN

October 18, 2016

Ms. Sarah M. Hayes, Chairperson  
Salem Retirement Board  
20 Central Street, Suite 110  
Salem, MA 01970

**REFERENCE:** Report of the Examination of the Salem Retirement Board for the three-year period from January 1, 2010 through December 31, 2012.

Dear Ms. Hayes:

The Public Employee Retirement Administration Commission has completed a follow-up review of the findings and recommendations contained in its audit report of the Salem Retirement Board for the period referenced above. We conduct these visits as a regular part of the oversight process. They are designed to ensure the timely implementation of corrective action for the recommendations cited in that report. The examination addressed six specific findings and recommendations included in the audit report for the period referenced above. The results are as follows:

***1. The Audit Report cited a finding that Regular Compensation Definition was not clear as The City of Salem had pay codes of “OT”, “Incentive”, “Detail”, “Extra”, “Clothing” and “Uniform” listed as qualified for retirement purposes.***

**Follow-up Result:** The Salem Retirement Board provided a document used in the Payroll Training conducted with each unit in the system. The document clearly provided examples of types of compensation that should be included or excluded from Regular Compensation. We reviewed the City of Salem weekly payroll report ending September 9, 2016 and searched for these specific pay codes. We noted the OT and Detail pay were properly excluded from regular compensation for pension purposes. We did not find any Incentive, Extra, Clothing or Uniform pay codes in use. This finding is resolved.



**2. The Audit Report cited a finding that there were issues with the calculation of the additional 2% contribution for compensation in excess of \$30,000. It was noted that five employees of the North Shore Regional Vocational High School and the City of Salem school department had new contracts that would result in their salaries exceeding \$30,000 thereby triggering the additional 2% contribution but the 2% deductions were not taken.**

**Follow-up Result:** We tested the same five employees with errors from the prior audit using the most recent payroll reports from July and August 2016. We found that one out of the five members did not have the correct 2% deduction taken in 2016. This employee was part of the North Shore Agricultural School. Per discussion with the Board, this was in error but will be corrected for the September 2016 payroll. We also tested 10 additional members from across all units including three from North Shore Agricultural School. We noted no calculation errors in the 10 additional test selections. **This finding is significantly resolved.**

**3. The Audit Report cited a finding that payroll records are not being used to calculate retiree benefits.**

**Follow-up Result:** We performed additional testing by selecting five retiree members who retired from various units in 2015. We found that for these five members the Board did verify payroll information. This finding is resolved.

**4. The Audit Report cited a finding that there were issues with the expenses of the system. The issues included duplicate payments from duplicate invoices, duplicate payments of single invoice, payments for same vendor and same service charged to different ledger accounts, insufficient descriptions for payments, and the Board was not using a standard reimbursement form that describes the nature, purpose and justification for reimbursement.**

**Follow-up Result:** As a result of the audit, the Board has started using sub-accounts in the general ledger to better organize expenses by vendor and service. We also noted the Board has started using a monthly Expenditure Report to compare Budget to Actual expenses. This review helps identify if expenses are charged to incorrect ledger accounts or if payments are duplicated. We reviewed the monthly warrants for 2015 and tested one expense from each month. We did not note any duplicate payments and found the sub-account helpful to organize the vendors and services. This finding is resolved.

October 18, 2016

Page Three

**5. The Audit Report cited a finding that Board staff was not delegating the calculation of unused sick time and vacation time buyback for Board staff members to an independent third party and applicable federal and state income tax were not properly withheld from staff members who previously had such buybacks completed.**

**Follow-up Result:** At the time of the follow-up, only one Board staff member was eligible for the sick time and vacation time buyback program and that staff member does not plan to retire in the near future. **This finding is not resolved due to the circumstances.**

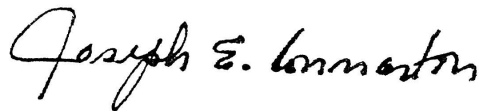
**6. The Audit Report cited a finding that a Board member did not meet the seventy-five percent minimum attendance threshold.**

**Follow-up Result:** We reviewed the Board's monthly minutes from 2013 through July 2016 and determined that all Board members were attending monthly meetings at or above the seventy-five percent minimum attendance threshold. This finding is resolved.

The Commission wishes to acknowledge the significant effort demonstrated by the staff of the Salem Retirement Board to correct the issues cited in the most recent examination of the system. PERAC auditors may conduct an additional follow-up visit to ensure appropriate progress is being made in those areas that have not been **fully** corrected at this time.

We anticipate your continued cooperation in resolving this important matter.

Sincerely,

A handwritten signature in black ink, reading "Joseph E. Connarton". The signature is fluid and cursive, with the first name "Joseph" being the most prominent part.

Joseph E. Connarton  
Executive Director

cc: Salem Retirement Board Members